Analysis

Are Finns living beyond their means?

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Finnish household consumption surpassed disposable income in 2016–2017. This has raised public concerns over household indebtedness. Is there a cause for concern, and how does household saving in Finland stack up against other countries? This article looks at the development of the household savings rate in Finland and compares this with household saving in other Nordic countries.

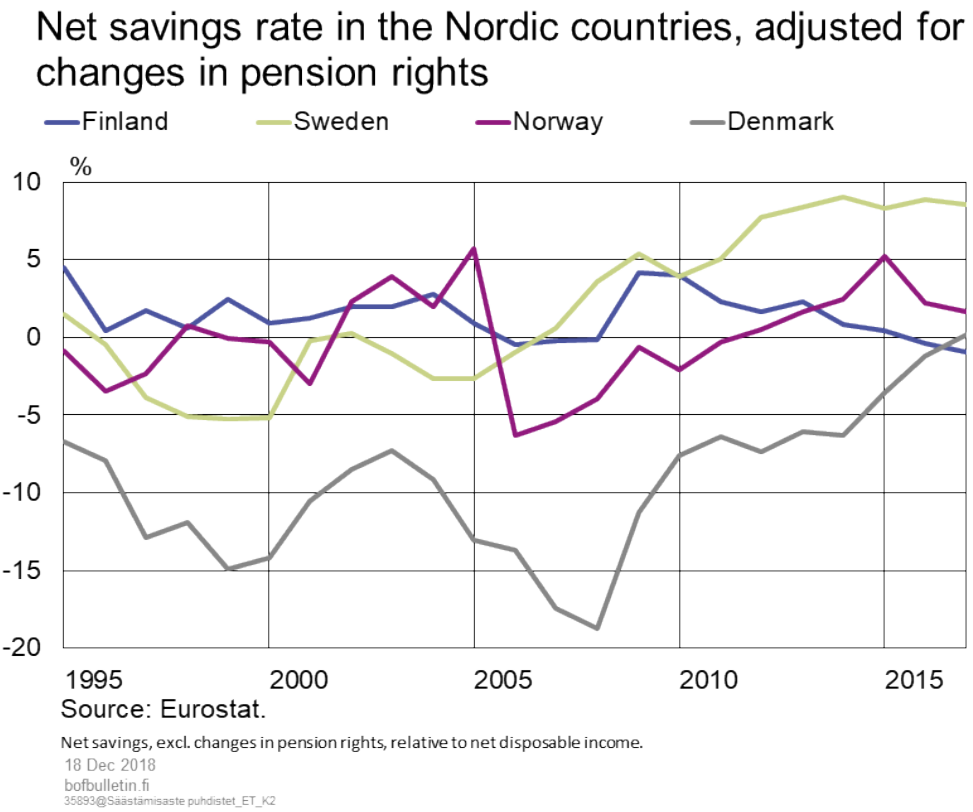


Household savings is the difference between disposable income and consumption expenditure. The savings rate is negative if consumption expenditure is higher than income. In that case, part of the expenditure must be financed by credit or realisation of assets. The savings rate is the ratio of household savings to disposable income. The net savings rate is a measure of savings that takes

into account also consumption of household fixed capital.

The household savings rate differs considerably across countries (Chart 1).[1] In 1995–2017, the net savings rate averaged 1.6% in Finland, but in Sweden was 9.2%. What is the reason for this large difference?

Chart 1.



The comparison of savings rates is hampered by cross-country differences in pension systems and statistics on pension savings. In some countries, the public sector assumes primary responsibility for ensuring that savings are collected for pension years, whereas in other countries the main responsibility falls on households themselves. Even in the case where the pension system is based on public sector savings, in national accounts, household savings include changes in the assets belonging to households under pension rights and gathered into the pension system. This applies however only if pension contributions are collected to finance future pension expenditure, i.e. the pension system is a funded system. If however, the pension system is a pay-as-you-go system in which the pension contributions collected in a period of time are used for paying current pensions, the pension contributions or pensions received are entered in the national accounts as tax-like charges and current transfers. The Finnish employment pension scheme is a partially-funded scheme, in which only some one-sixth of the collected pension contributions are saved into a fund.

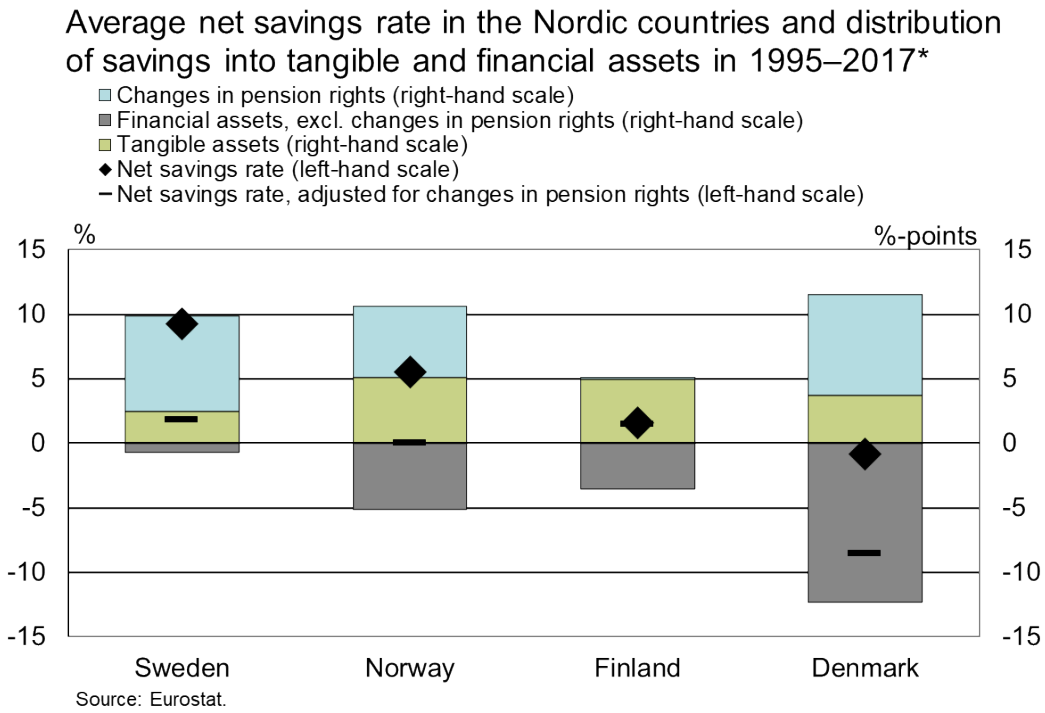
The national pension system is a pure pay-as-you-go system, which is funded by government tax revenues.

A comparison of savings rates that have been adjusted for savings resulting from changes in households' pension rights shows that changes in pension rights have a significant impact on the household savings rate (Chart 1). The impact is particularly large in countries in which the pension system's funding rate is high or in which supplementary pension systems (these are usually fully-funded) are extensively used, for example in Sweden and Denmark. In these countries, the savings rate, adjusted for changes in pension rights, is considerably lower than the observed savings rate, and a large part of household saving takes actually place via the pension system. In 1995–2017, the net savings rate that takes into account differences in the pension systems was in Sweden on average 1.8%, in Finland 1.4%, in Norway 0.0% and in Denmark as low as −8.6%. Compared with its Nordic peers, Finnish households' savings rate has thus not been that low on average.

The savings rate however does not show the distribution of household savings between the various forms of wealth. Despite the low savings rate, households may continue to accumulate wealth. Finnish households invest the bulk of their savings in tangible assets, mainly housing (Chart 1). At the same time, this accumulation of assets has been financed with credit, in which case savings in financial assets has been negative. In other words, the household sector has been a net borrower. Finnish households' average rate of savings in tangible assets was 4.9% in 1995–2017. The figure for Norway is 5.1%, Denmark 3.7% and Sweden 2.4%. The volume of savings in tangible assets – in practice housing, is thus virtually as large as in for example, Denmark and Norway. However, in Denmark the average volume of net borrowing by the household sector has been considerably larger than the accumulation of tangible assets, which indicates that households have for a protracted period financed their consumption expenditure either by taking out credit or via realisation of assets.

Since 2010, the savings rate in Finland has however demonstrated a downward trend, in contrast to the other Nordic countries (Chart 2). In 2017, Finland's savings rate, adjusted for changes in pension rights, was the lowest of the four countries, i.e. −1.0%. The downward trend in Finland is due to the increasing amount of debt accumulated by households relative to disposable income in 2010–2017, in other words, net financial assets have declined continuously (Chart 3). However, households have not accumulated tangible assets at the same pace. Thus in recent years, households have lived beyond their means: household consumption expenditure has exceeded the amount of disposable income, and households have financed the growing volume of consumption either by selling their assets or by taking out credit, supported by low interest rates.

Chart 2.

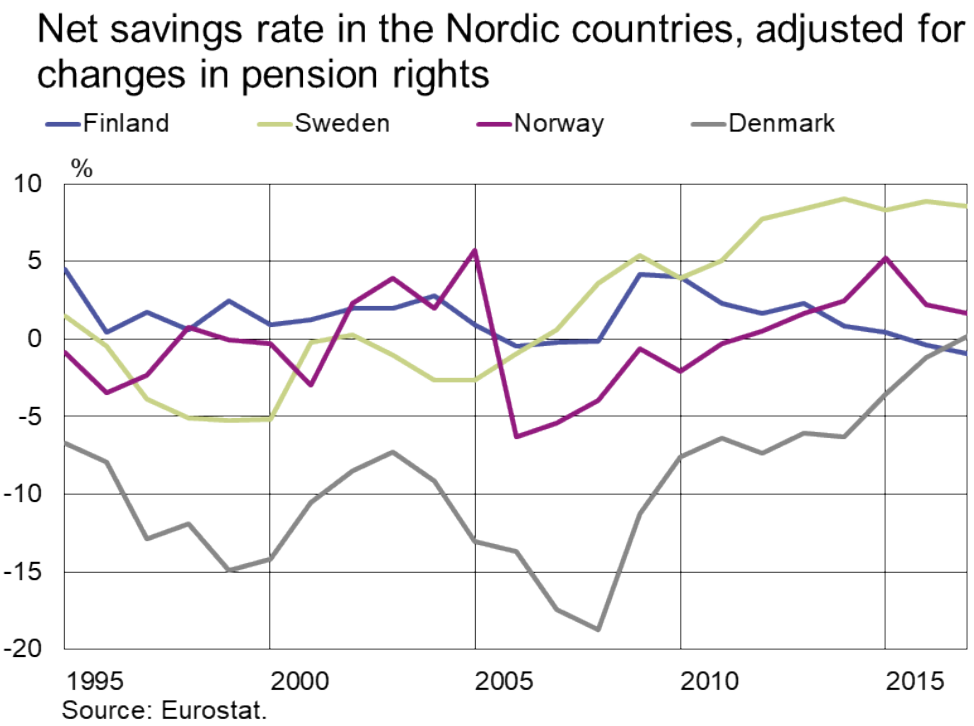


Source: Eurostat.

**The savings rate is decomposed into savings in financial assets and tangible assets, relative to disposable income. Tangible assets consist mainly of real property, valuables and natural resources. Savings in financial assets is further divided into changes in pension rights and changes in other net financial assets, i.e. the difference between assets and liabilities.*

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Chart 3.



Notes

1. For a similar examination, based on 2012 data, see Stijn Rocher and Michael H. Stierle: Household saving rates in the EU: Why do they differ so much?, European Economy Discussion Paper 005, European Commission 2015. ↑

Keywords

consumption, households, indebtedness, savings ratio